MULTIMEDIA UNIVERSITY

STUDENT ID NO

MULTIMEDIA UNIVERSITY

FINAL EXAMINATION

TRIMESTER 2, 2017/2018

BAC2644 – CORPORATE FINANCE

(All sections / Groups)

6 MARCH 2018
2.30 p.m –5.30 p.m
(3 Hours)

INSTRUCTIONS TO STUDENTS

1. This question paper consists of **FOUR(4)** printed pages.
2. Answer **ALL** questions.
3. Marks are shown at the end of each question.

QUESTION 1 (25 marks)

a) PG PLC is considering investing in a new project in Canada which will have a life of 4 years. The initial investment is C$120,000 including working capital. The net after tax cash flows which the project will generate are C$70,000 per annum for years 1,2 and 3 and C$55,000 in year 4. The terminal value of the project is estimated at C$40,000, net of tax.The current spot rate of Canadian dollars against the pound sterling is 1.7000 C$/£.Economic forecasters expect the pound to strengthened against the Canadian dollar by 5% per annum over the next 4 years. The company evaluates UK projects of similar risk at 14%.Calculate the NPV of the Canadian project .

(10 marks)

b) Currently shareholders' wealth maximization is the major goal of ABC Limited. Nonetheless the directors think that management should also give emphasis on several factors that influence firms operating activities such as:

a) Cash flow generation
b) Risk adjusted returns to shareholders
c) Performance improvement in a number of areas such as concern for the environment , employees' remuneration and quality of working conditions and customer satisfaction

Required:
Provide the managing director (MD) with a report for the presentation at the next board meeting, which evaluates the argument that maximization of shareholder wealth should be the only true objective of the company, and discuss the advantages and disadvantages of the MD's suggestions about alternative goals.

(15marks)

Continued...

QUESTION 2 (25 marks)

a) Anasz Co is a company, which installs cabinet in the Klang Valley. It plans to extend its business covering the outskirts in the valley and need RM 2,760,000. The sales orders for the next four years are 400 units. The sales of the cabinet depend on the state of the economy and probability of its selection. The selling price and conversion costs depend on the states of the economy. The fixed cost for this project is RM 280,000.

Economic probability	Probability of Selection	Selling price (RM/unit)	Conversion costs (RM/unit)
Worst	15%	38,600	25,580
Normal	65%	46,700	29,000
Boom	20%	65,900	43,000

Anasz pays corporate tax of 28% per year, with the tax paid in the year it incurred. Depreciation is calculated based on the straight-line basis, and company can claim tax allowance depreciation on the cost of investment over the ten years. Anasz used an after tax discount rate of 18%. Calculate the Net Present Value of the planned investment.

(14 marks)

b)A portfolio has 25% of its funds invested in Security C and 75% of its funds invested in Security D. Security C has an expected return of 8% and a standard deviation of 6%. Security D has an expected return of 10% and a standard deviation of 10%. The securities have a coefficient of correlation of 0.6. Calculate the portfolio return and variance.

(5 marks)

c) What is the expected return on a portfolio, which is invested 20% in stock A, 50% in stock B, and 30% in stock C?

State of the economy	Probability of State of Economy	Return if state occurs		
		Stock A	Stock B	Stock C
Booms	20%	18%	9%	6%
Normal	70%	11%	7%	9%
Recession	10%	10%	4%	13%

(6 marks)

Continued...

QUESTION 3 (25 marks)

a) An electric equipment manufacturing company is unlevered. They are currently deciding whether including debt in their capital structure would increase their value. Under consideration they can borrow new debt at 6.5 percent. The firm's WACC is currently 12 percent. There are currently 32,000 shares outstanding and the firm is considering a new capital structure by converting to 45 percent debt. Assume that the corporate income tax rate is 35 percent and the marginal tax rate for the average shareholder is 25 percent. Assume that the manufacturing company has a new debt-equity ratio of 2.5. Calculate the followings figure:

(i) The manufacturing company cost of equity capital.

(5 marks)

(ii) The company unlevered cost of equity capital.

(5 marks)

(iii) The electric equipment manufacturing company new weighted average cost of capital (WACC).

(5 marks)

b) Establishing a capital structure for a firm is not simple. Although financial theory guides the process, there is no simple formula. Nevertheless, Modigliani-Miller and Packing-Order theories are considered as well-known in determining the capital structure. List and explain Modigliani-Miller's proposition I and proposition II in the area of capital structure.

(5 marks)

c) Suppose that on November 2, 2016, a Malaysian company sold goods to a German company for €1=$1.160. On that same day, the Malaysian company entered into a forward contract to sell € 100,000 in 90 days at €1= $1.162. Discuss the risk exposure of this Malaysian company by trading with a German company.

(5 marks)

Continued...

QUESTION 4(25 marks)

a) Yeasmin Sdn. Bhd's financial statement information is given hereunder in the table:

Item	Beginning (RM), 2017	Ending (RM), 2017
Inventory	11,780	13,380
Accounting receivables	5,320	6,070
Accounts payable	7,536	7,999

Credit sales for the period just ended were RM90,750 and costs of goods sold in 2017 were RM66,284. Other expenses are expected to be RM15,000 per month. Assume a '365-Day' year. Calculate the Operating Cycle (OC) and Cash Cycle (CC) of the Yeasmin Sdn. Bhd. for the year 2017. How do you interpret your answer?

(10 marks)

b) You have recently been appointed as a Chief Financial Officer of Papri Sdn. Bhd. You are asked to discuss the following in the coming top management committee meeting: 'Short-term Financial Policy', 'Carrying Costs Vs. Shortage Costs', and 'Cash Budget'.

(9 marks)

c) Blue Occean Berhad is analyzing the possible acquisition of Chan Sdn. Berhad. Both firms are unlevered. The forecasts of Blue Occean Berhad show that the purchase would increase its annual after-tax cash flow by RM 365,000 indefinitely. While the current market value of Chan Sdn. Berhad is RM 12 million, the current market value of Blue Occean Berhad is RM 21 million. The appropriate discount rate for the incremental cash flows is 10 percent. Blue Occean Berhad is trying to decide whether it should offer 30 percent of its stock or RM20.5 million in cash to Chan Sdn. Berhad. As a Chief Financial Officer, you are asked to answers the following:

i) What is the synergy from the merger?

(3 marks)

ii) What is the purchase price to Blue Occean of each alternative?

(3 marks)

End of Paper